

Bill Baxter, Chairman

Tennessee Valley Authority

March 8, 2006

**Testimony of
Bill Baxter
Chairman, Tennessee Valley Authority
before the
House Transportation and Infrastructure Committee
Subcommittee on Water Resources and Environment**

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Opening Statement

Chairman Duncan, Ranking Member Johnson, and members of the Committee, it is an honor to appear before you today. I was appointed by President Bush to the TVA Board in November 2001 and named Chairman on June 16, 2005. On behalf of Director Skila Harris and TVA's dedicated employees, I would like to thank you for this opportunity to discuss TVA's priorities and goals for the coming fiscal year.

Director Harris and I look forward to welcoming seven new TVA Board members as part of a change in the leadership structure of TVA. On March 3rd, the United States Senate confirmed the President's nominations of six people to serve on the expanded nine-member TVA Board. Once they are sworn in, these new Board members, along with Director Harris and myself, will consider long-term policies and goals for TVA and select a Chief Executive Officer to run the day-to-day business. I look forward to this new structure, which I believe will help prepare TVA for its future in a changing environment.

Building on our Momentum

TVA is a wholly owned corporation of the United States government that provides reliable, competitively priced electric power to 8.6 million residents of a seven-state region. We sell electricity wholesale to 158 local utilities and directly to 61 large industrial customers and federal installations. Additionally, TVA serves as a steward of the region's natural resources and a catalyst for sustainable economic development. In the three key areas of energy, environment, and economic development, TVA generates momentum, helps our region thrive, and improves the quality of life in the Tennessee Valley.

In preparing for the future, we at TVA are building on this momentum and are committed to a disciplined approach to improving our financial flexibility.

Affordable, Reliable Power

TVA fuels the region's economy by supplying reliable, affordable electric power to the Tennessee Valley through a diverse portfolio of generating assets. The TVA electric power system includes 11 coal-fired plants, three nuclear plants, 29 hydro-electric plants and five combustion-turbine plants. In addition to traditional generation sources, TVA's Green Power Switch Program employs wind, solar, and methane-gas generation to offer many consumers in the Valley the option of purchasing renewable power from their local power distributors.

The President's Advanced Energy Initiative recognizes the value of using diversified, domestic sources of energy. TVA is an example of the power of such diversification. By using a balance of coal, nuclear, gas, hydro-electric, and renewable sources of energy, TVA is doing its part to ensure the long-term reliability and affordability of electric power in the Southeast.

In 2005, TVA's generation and transmission system had its most successful year on record. The TVA transmission system is a critical link in the movement of electricity throughout the eastern United States. In 2005, the TVA system provided our customers with more than 171 billion kilowatt hours of electricity. For the sixth year in a row, the system delivered power to our customers with 99.999 percent reliability. The power system also met back-to-back all-time peak demands during one week in July. The second peak, which measured 31,924 megawatts, was 6.5 percent higher than any previous TVA peak.

During the year, TVA's coal-fired plants generated 98.4 billion kilowatt-hours of electricity, four percent above last year's total, and achieved their best reliability ever recorded for a fiscal year. In our nuclear operations, TVA's nuclear plants achieved their best-ever record for equipment reliability in 2005, and the industry publication *Nucleonics Week* ranked Browns Ferry and Sequoyah first and second in the U.S. for the lowest average operating and maintenance costs reported by nuclear utilities for the years 2002 through 2004. Our nuclear program is also supporting TVA's historic role in national defense. In 2001, TVA and the Department of Energy signed an agreement to use surplus highly enriched uranium (HEU) as a source of fuel for TVA reactors. The HEU is blended to low enriched uranium (BLEU) in order to eliminate it as weapons-usable fissile material and to provide fuel for TVA's Browns Ferry nuclear reactors. In 2005, TVA's BLEU program won a Platts Global Energy Award as the Energy Engineering Project of the Year.

Anticipating the future power needs of the Tennessee Valley, we are working hard to make our power system even stronger. We expect power needs in the region to increase an average of two percent every year in the coming decade. To help meet this need, TVA will bring online the nation's first nuclear reactor of the 21st century. Browns Ferry Unit 1, located in Athens, Alabama, is on budget and on schedule to go into service in May 2007. It will provide 1,280

megawatts of safe, zero-emission base-load generation. These megawatts will not only add about four percent to our generating capacity, but will also be cheaper than our average cost of generating power.

To ensure a reliable power supply for the long-term, we are also exploring potential advances in nuclear power through the 11-company NuStart Energy Development consortium, which is developing the design certification and licensing of two advanced nuclear power reactors.

Environmental Stewardship

As steward of the Tennessee Valley's natural resources, TVA is continuing to improve the way we manage the Tennessee River watershed and the aggressive emissions-reduction program we are implementing to make the region's air cleaner.

The Tennessee River is the backbone of the Valley. Managing the river system – the fifth-largest in the United States – is at the heart of TVA's mission and requires a careful balance of stakeholder needs. In 2005, TVA's new policy for operating the river system helped us meet flow commitments, keep water levels higher through Labor Day for recreation, and generate much-needed hydropower to meet electricity needs.

Due in part to our ongoing hydro-modernization program, TVA dams generated 15.7 billion kilowatt-hours in Fiscal Year 2005, which was 13 percent above normal. At the same time, TVA used its series of locks and navigation channels to help transport some 50 million tons of cargo by barge, saving shippers \$550 million over alternative forms of transportation.

We are also working to ensure that the Tennessee Valley's air will be cleaner for our children and grandchildren. Air quality in the TVA region is the best it has been in decades, according to air-quality trend studies by the Environmental Protection Agency. Last year, TVA spent \$202 million on clean air equipment. TVA currently expects to add five sulfur-dioxide scrubbers to the six already in use at its coal plants, and two are currently under construction. When all 11 are complete, TVA's sulfur-dioxide emissions will be 80 to 85 percent below levels in the historical peak year of 1977.

In 2005 we also added two new nitrogen-oxide selective catalytic reduction (SCR) systems to our coal-fired plants. With 20 SCRs now in operation, nitrogen-oxide emissions have been lowered 80 percent since the historical peak year of 1995. When our current commitments are completed, we expect to have invested \$5.7 billion to reduce emissions. This is one of the most aggressive clean-air programs being carried out by any utility in the country.

Economic Development

TVA is also keeping up the momentum of economic development in the Valley. By partnering with public officials and communities, we have helped the region to attract and keep quality jobs. In 2005, along with our state and local partners, TVA helped attract or retain over 57,000 jobs and leverage almost \$3.6 billion in capital investments in the region.

One initiative that will boost the region's economy for years to come is the Megasite Certification Program. This program certifies large industrial properties as "megasites," suitable for major automotive or other large manufacturing facilities. In November, the first industrial investor decided to locate a plant at one of five certified megasites.

In addition to the technical assistance and low-interest loans that TVA provides to communities working to attract new businesses, in 2005 we offered specific tools to communities interested in recruiting life sciences industries and retail/commercial development.

TVA's economic development partnerships, along with reliable and competitively priced electric power, help make the Valley region a great place to do business.

Reduction in Total Financing Obligations

At the same time that TVA is striving to achieve operational excellence, be effective stewards of our natural resources, and promote economic development in the Tennessee Valley, we are committed to increasing our financial flexibility. To achieve that goal, TVA must reduce its Total Financing Obligations (TFOs), which include both statutory debt and such alternative financing mechanisms as lease-leasebacks and prepayment agreements.

Since the end of 1996, TVA has reduced its Total Financing Obligations by \$2.1 billion. In FY 2005, TVA reduced them by \$301 million, \$76 million more than was budgeted. The amount of each revenue dollar used to pay interest and other financing expenses has declined from 34 cents to 18 cents. The TVA Board remains committed to the trend of reducing our financing obligations and will continue to work with the Administration and Congress on our goals for achieving greater financial flexibility.

In fact, TVA is striving to reduce our financing obligations even more than was called for in the TVA Strategic Plan released in 2004. In FY 2007, we plan to reduce Total Financing Obligations by \$529 million to help us reach our goal of a \$7.8 billion reduction by 2016. TVA believes it can meet this goal if we work to constrain our Operations and Maintenance costs and if TVA can recover from

customers the increased fuel and purchased power costs that we, like utilities across the country, are experiencing.

FY07 Budget Overview

TVA's power program is entirely self-financing and does not receive federal appropriations. TVA projects revenue in FY 2007 of more than \$9 billion, including two recent rate adjustments approved by the Board to recover the fuel and purchased power costs.

We have been working closely with our distributor customers on the problems associated with rising fuel costs, and we are continuing to work with them on long-term solutions. We are making internal cost reductions to offset some of the increases, and we must pass along some of the costs to our customers. We appreciate our customers understanding the problem of rising fuel costs and that this national problem is coming at us from three sides.

- First, coal prices are up significantly. Some major coal suppliers are experiencing multiple production and transportation problems.
- Second, natural gas prices have also increased dramatically. Prices were driven up by the two hurricanes in the Gulf last fall, which affected natural gas supplies. In fact, natural gas supplies from the Gulf are still running below normal.
- Third, higher coal and natural gas prices drive up the price of power we buy on the bulk power market. Right now, we buy that power to meet some peak demands and to continue fueling the Valley's growing economy. In 2005, we acquired about 12 billion kilowatt-hours – or about seven percent of our total sales for the year – through such purchases. On a positive note, when we bring Browns Ferry Nuclear Plant Unit 1 on-line in 2007, it will reduce our need for purchased power.

In Fiscal Year 2007, TVA will spend approximately \$1 billion in capital projects for the power system, including \$306 million for clean air projects, \$81 million for Browns Ferry Nuclear Plant Unit 1, and \$209 million for transmission system reliability.

TVA continues to effectively operate and maintain its systems of dams, reservoirs, and adjacent lands. Beginning in Fiscal Year 2000, TVA has funded its stewardship activities solely out of power revenues, user fees, and sources other than appropriations. In FY 2007, TVA will spend approximately \$84 million on water and land stewardship activities.

Beginning with our annual report for FY 2006, TVA will begin filing financial reports with the SEC, in accordance with the Consolidated Appropriations Act, 2005. In FY 2007 we will also begin complying with portions of the Sarbanes Oxley Act to ensure that TVA is providing the appropriate level of disclosure and transparency for its stakeholders.

Conclusion

TVA is in a time of transition, and I believe TVA's new structure of a nine-member Board of Directors and a Chief Executive Officer to run the day-to-day business will help lead TVA into the future. It is also important to note what is not changing at TVA, and that is TVA's dedication to its mission of service to the Tennessee Valley region.

TVA remains committed to reducing Total Financing Obligations and to achieving our mission of delivering reliable, affordable electric power; efficiently managing the Tennessee River system; and supporting sustainable economic development in the region. We will continue to work with the Congress, the Administration, and all of our stakeholders to ensure that we accomplish these goals.

Thank you again for the opportunity to appear before you today, and I look forward to answering any questions you may have.